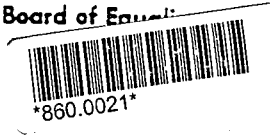
State of California

Board of Equ...



Memorandum

To : Mr. L. Gene Mayer

Date : January 16, 1987

From : Ken McManigal

Subject : Assessment Responsibility on Railcar Repair Facilities

This is in response to your November 17, 1986, memorandum wherein you advised that General Electric Company had recently purchased North American Car Company's railcar fleet and repair facilities, had had its General Electric Railcar Services Co. subsidiary take ownership of and operate the railcar fleet, and had had its Quality Service Railcar Co. subsidiary take ownership of and operate the repair facilities; and you asked whether the Valuation Division should retain assessment jurisdiction of the repair facilities, which it had when both the railcar fleet and the repair facilities were owned by North American Car Company, or return assessment jurisdiction of such facilities to county assessors.

We believe that the Valuation Division should return assessment jurisdiction of the repair facilities to the appropriate county assessors. Article XIII, section 19 of the California Constitution provides in this regard that the Board shall annually assess property owned or used by car companies operating on railways in the state. As structured by General Electric Company, the car company operating on railways in California is General Electric Railcar Services Co., a subsidiary separate and distinct from the Company itself and from its other subsidiaries, including its Quality Service Railcar Co.; and thus, the Valuation Division should retain assessment jurisdiction over only that property owned or used by General Electric Railcar Services Co., primarily the railcar fleet.

Attached for your general information is a copy of an October 22, 1986, letter from Ms. Barbara Elbrecht to Mr. Max Goodrich which addresses the relationship between a parent corporation and its subsidiary corporations, sets forth and discusses circumstances under which corporate entities/subsidiary entities might be disregarded, and concludes that in light of

the available information there is no basis for disregarding the separate existence of the parent corporation and its subsidiaries. In the same vein, there is nothing to suggest that the separate existence of General Electric Company, General Electric Railcar Services Co., and/or Quality Service Railcar Co. should be disregarded in this instance.

JKM/rz

Attachment

cc: Mr. Richard Ochsner
Mr. Gordon P. Adelman
Mr. Robert Gustafson
Mr. Gene DuPaul
Mr. Octavio Lee
Mr. Chad McDonald
Legal

0391H

Memorandum

To : Mr. Richard Ochsner Date : November 17, 1986

From : Louis E. Mayer, Chief
Valuation

Subject : Assessment Responsibility on Railcar Repair Facilities

In 1986 and prior years we have assessed repair facilities owned by North American Car Company. These facilities, along with a railcar fleet, have been sold to General Electric Co.

Two separate subsidiaries have been set up by General Electric Company:

General Electric Railcar Services Co. which operates the railcar fleet

Quality Service Railcar Co. which operates the repair facility

Gene DuPaul of my staff and Ken McManigal of yours participated in a meeting with Richard Althoff of General Electric to discuss this and other issues connected with the sale. Gene concludes, and believes Ken agrees, that we should return assessment jurisdiction for these two shops to the county assessors.

This action would be consistent with the Board's earlier treatment of Trailer Train's repair facility when it was operated by a subsidiary. The reason would be that there is not a strong enough connection between the two companies to meet the "owned or used by" criteria in Article XIII Sect. 19.

If you concur, we will advise the company and the two county assessors of this decision.

LEM:GD:js

cc: Mr. Gordon Adelman
Mr. Robert Gustafson
Mr. Ken McManigal
Mr. Gene DuPaul
Mr. Octavio Lee
Mr. Chad McDonald

STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
1020 N STREET, SACRAMENTO, CALIFORNIA
P.O. BOX 1799, SACRAMENTO, CA 95808)
916/454-6593

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Executive Secretary

October 22, 1986

Mr. Max Goodrich
Chief-Ownership, Exemption &
Mapping Division
Los Angeles County Assessor
500 West Temple Street
Los Angeles, CA 90012

RE: Exemption Provided for Vessels Engaged in Transportation

Dear Mr. Goodrich:

This is in response to your letter of July 7, 1986, to Mr. Richard H. Ochsner wherein you request our opinion regarding the applicability of the exemption from taxation provided by Section 3(l) of Article XIII of the California Constitution to vessels used by a subsidiary corporation to transport for hire the property of a parent corporation. The facts provided in your letter and the accompanying memoranda from the Office of the County Counsel can be summarized as follows:

> The S. S. Coast Range and the S. S. Sierra Madre were both built in San Diego by National Steel and Ship Building Company and delivered to Union Oil Company of California ("Union") on October 29, 1981, and December 18, 1981, respectively. Both vessels were bareboat chartered by Union to West Coast Shipping Company ("West Coast"), a wholly-owned subsidiary of Union, for $550,000 per month. (Bareboat Charter Parties, p. 7.)
>
> West Coast with its staff of 28 employees operates both state-of-the-art vessels as product carriers under transportation contracts with Union, delivering together more than nine million barrels per year of Union's products to west coast markets. It also operates two other ships regarding which we have no information.
>
> Two virtually identical transportation contracts between West Coast and Union dated September 29, 1981, (for the S.S. Coast Range) and December 15, 1981, (for the S.S. Sierra Madre) require West Coast, the carrier, to provide to Union, the shipper, the two tank vessels for the

has the right to name the vessels, display its insignia on the vessels' stacks, fly its house flag and determine the color of paint and the general scheme thereof on the vessels. (Transportation Contracts, p. 1).

The amount of freight agreed to by contract was the sum of all costs to the carrier, including all paid under the charter, plus a management fee. The shipper agreed to indemnify the carrier against all liabilities in excess of the carrier's insurance coverage, except for fraud, willful misconduct or criminal acts. (Transportation Contracts, p. 8)

The complex job of planning and coordinating the West Coast shipping operations is handled at the West Coast office, located in Union's 911 Wilshire building. "Unocal [Union] has an individual who keeps track of inventories at marketing terminals and production at the refineries.... He lets [West Coast] know what's needed at each location, as well as what each wants to move--when, where and in what amounts. We then take those requirements and try to fit them into a schedule that will satisfy the marketing people, and the limitations of the vessels." (Seventy Six, Jan.-Feb. 1986, p. 11).

Union has stated "[t]he reasons for utilizing a separate Union subsidiary to operate the vessels, rather than having Union operate the vessels directly, are the same as those which are involved in the utilization of an unrelated transportation company: the limitation of liability and the avoidance of complex labor problems which would be associated with direct operation (Letter, May 15, 1986, from Michael A. Lovett, Unocal).

The "Arco California," an oil tanker, is owned by Arco Marine, Inc., a wholly-owned subsidiary of Atlantic Richfield Company. It was purchased from National Steel and Shipbuilding Company on July 15, 1980.

The information available to us indicates the Arco California transported crude oil for hire for the period from March 1, 1981, through March 1, 1985, for several different oil companies, including 1) ARCO Petroleum Products Company, 2) British Petroleum, 3) Champlin, 4), Chysen, 5) Shell, 6) Sohio, and 7) Unocal. No information has been provided about the relative amount of time per shipper.

County Counsel, in a memorandum dated June 3, 1986, has stated that the information provided by Union is persuasive regarding the issue of whether the exemption provided by

Section 3(1) of Article XIII applies to the S.S. Coast Range and the S.S. Sierra Madre, but that a court may examine the facts in a property tax context and decide to disregard the separate corporate entity of the subsidiary. Such disregard of the separate nature of parent and subsidiary would defeat the claim for exemption. However, additional information on the ARCO California was requested by County Counsel in a memorandum dated July 26, 1985, before making any determination about the applicability of the exemption to the Arco California.

Analysis

Section 3(1) of Article XIII of the California Constitution exempts from property taxation:

> Vessels of more than 50 tons burden in this State and engaged in the transportation of freight or passengers.

The phrase "engaged in the transportation of freight or passengers" has been construed by the California courts to mean the carrying of freight (property transported by a carrier from a consignor to a consignee) or passengers (travelers by some established conveyance) for hire (Dragich v. Los Angeles (1939) 30 Cal.App.2d 397). Thus, the question presented is whether these subsidiary corporations are independent corporations that ship the products of Union and the other petroleum companies for hire, or whether the subsidiary corporations are mere instrumentalities, conduits or agents for the parent corporations. If the corporate entity of the subsidiary corporation can be disregarded, the parent and subsidiary can be treated as one unit, thus defeating any claim that the vessels are transporting freight for hire.

The "alter ego" doctrine, the disregard of the corporate entity because the corporation is the alter ego of others, is applicable not only where the corporation is the alter ego of individuals forming or owning it, but also where a corporation is so organized and controlled, and its affairs so conducted, as to make it merely an instrument, agent, conduit or adjunct of another corporation (McLoughlin v. L. Bloom Sons Co., Inc. (1962) 206 Cal.App.2d 848). "With increasing frequency, courts have demonstrated a readiness to disregard the corporate entity when a wholly-owned subsidiary is merely a conduit for, or is financially dependent on, a parent corporation" (1B Ballentine & Sterling, Calif. Corp. Laws, ¶ 296.01, p. 14-33). Although the doctrine has been applied largely in tort and contract cases to assure a just and equitable result (Thomson v. L. C. Roney & Co. (1952) 112 Cal.App.2d 420; 1A Ballentine & Stirling, Calif. Corp. Laws, ¶ 295, p. 24-31), the doctrine has

been found applicable to state tax matters to prevent the circumvention of revenue and tax laws (People v. Clauson (1964) 231 Cal.App.2d 374). Factors which the courts have evaluated to determine if the separate existence of the subsidiary corporation should be disregarded are:

1. Presence in both corporations of the same officers or directors.

2. Joint accounting and payroll systems.

3. Subsidiary's lack of substantial business contacts with any save the parent.

4. Subsidiary operates solely with assets conveyed by parent.

5. Subsidiary is shown as a division on parent's financial statements.

6. Subsidiary's property is used by the parent as its own.

7. Subsidiary acts in interest of the parent.

(Annot. (1963) 7 A.L.R.3d 1343, 1355)

Based on the facts presented here, it is difficult to sustain the conclusion that the separate existence of West Coast and Union can be disregarded. Union formed a separate subsidiary corporation to operate the vessels for legitimate business purposes: to limit liability and to avoid complex labor problems which would be associated with direct operation. Union treated West Coast as a separate entity, as shown in the Bareboat Charter Parties in which West Coast leased the two vessels from Union and in the Transportation Contracts in which West Coast agreed to ship Union's products for a specified sum. Moreover, West Coast has two additional vessels about which we have no information, which may be utilized in ways that further support Union's claim that West Coast is an entity separate from Union. Therefore, unless substantial additional evidence is provided to show that West Coast is a mere instrumentality of Union, such as the listing of West Coast as a division of Union rather than a subsidiary corporation on Union's financial statements, or the parent used the assets of the subsidiary as its own without regard to corporate formalities, we believe there is insufficient evidence to treat West Coast as the alter ego of Union. Consequently, the exemption provided by Section 3(1) of Article XIII is applicable to the vessels S.S. Coast Range and S.S. Sierra Madre.

Moreover, the evidence you have presented regarding the subsidiary status of Arco Marine, Inc. also does not provide sufficient support for disregard of the corporate entity. The Arco Marine, Inc.'s vessel, the ARCO California, transports the products of the several oil companies named above, including its parent Atlantic Richfield, and appears to be engaged in the transport of freight for hire. Based on this little evidence, we cannot state that the exemption is inapplicable to the ARCO California.

I trust that the above information has been of service to you. If you have any further questions, please do not hesitate to contact me.

Very truly yours,

Barbara G. Elbrecht

Barbara G. Elbrecht
Tax Counsel

BGE/rz

cc: Mr. Gordon P. Adelman
Mr. Robert Gustafson
Mr. Verne Walton

0147H

State of California Board of Equalization

Memorandum

To : Mr. Verne Walton Date : January 21, 1992

From : James M. Williams

Subject : Vessel Exemption, Cal. Con., Article XIII, Section 3( )

In your memo of November 1, 1991 you posed five questions for our opinion. Prior to responding I want to make clear that I am not opining on whether or not the vessels of the Dutra Construction Company qualify for the subject exemption. If that is desired, the taxpayer should file the appropriate claim in the manner prescribed. A description of the employment of each vessel, as indicated in Smith-Rice Heavy Lifts, Inc. v. Los Angeles Co. (1967) 256 Cal. App. 2d 190, is required for proper evaluation of the claim. The assessor is not required to sift through two hundred pages of irrelevant United States Army Corps of Engineers' form contracts to act on the taxpayer's claim.

1. What cargo qualifies as freight? What does not?

Response: "In holding that a commercial fishing vessel transporting its catch to its home port was not engaged in the transportation of freight, the court refused to accept the argument that "freight" means "any property" stating: The word "freight" has more than one meaning but it generally denotes property transported by a carrier from a consignor to a consignee." Crowley Launch and Tugboat Co. v. County of Los Angeles (1971) 16 Cal. App. 3d 437 at page 440.

2. What constitutes regular engagement in the transportation of freight?

Response: The vessel should be designed and constructed for the transportation of freight and it should be exclusively used for that purpose. It may be temporarily withdrawn from active use for repairs or for lack of business but not for diversion to another use. In this instance the vessel was laid up for seven months of the year, including the lien date, because of lack of business. Los Angeles Co. v. Craig (1940) 38 Cal. App. 2d 58.

3. Is a consignor-consignee relationship needed for the assessor to grant the exemption?

Response: Although the response to question 1. may seem to indicate the necessity of a consignor-consignee relationship, it does not quite go to a 100% requirement. Note that the court inserted the word "generally". The seminal case interpreted the section to read:

> Vessels of more than 50 tons burden in this State and engaged in the transportation of freight or passengers -- for hire.

Thus the catch of one's own fishing boat is not freight but hauling another's catch for a fee would qualify without the full necessities of a consignment. Dragich v. Los Angeles Co. (1939) 30 Cal. App. 2d 397.

4. Do the enclosed contracts and documents support a consignor-consignee relationship?

Response: I could not so ascertain. I kept getting lost in federal boiler plate. I can tell you that no drugs are involved because the contracts contain a clause requiring a drug free environment.

5. Would these vessels qualify for exemption based on the freight definition used for property taxes?

Response: I don't know what the definition of freight is for property taxes. Also I can not ascertain how many vessels are involved and how each is engaged; see my first paragraph about filing the appropriate claim. If, in general, the taxpayer's vessels are (1) carrying rocks owned by the taxpayers to a site of levee-repair or (2) carrying dredged materials from a ship channel wherein the taxpayer was hired to complete the entire project, then these engagements do not qualify under Dragich cited above or Crivello v. San Diego Co. (1942) 50 Cal. App. 2d 713.

Hopefully these responses will give you some idea of how the courts have interpreted this exemption. However, if the taxpayer wishes to go further, he should follow the claim procedures and make available the appropriate, detailed information.

JMW:jd
4324H

(916) 445-4982

January 31, 1980

Honorable Jack M. Waterman
Ventura County Assessor
800 S. Victoria Avenue
Ventura, California 93009

Attention: Mr. Peter H. Finie
Marine/Aircraft Appraiser

Dear Pete:

We are writing in response to your recent inquiry regarding the exemption of vessels.

Your first question involved a vessel over 50 tons burden under contract to ferry drilling crews to and from offshore drilling facilities. You ask whether this activity would qualify the vessel for exemption under Article XIII, Section 3(L) of the California Constitution. The reason you question the vessel's eligibility for exemption is because the vessel is not hauling passengers in the normal sense.

In Star and Crescent Boat Co. v. San Diego County, 163 Cal. App. 2d 534, tugboats were under contract to pull barges filled with petroleum products. The court held that the tugs were hauling freight for hire and eligible for exemption. Based on the findings in this case, we suggest that the vessel in your inquiry would be eligible since the vessel is commercially engaged in hauling people to and from given points, even though, as you point out, the vessel is not available to haul passengers generally.

The same reasoning would apply to your second question regarding the vessel under contract to haul supplies and equipment to the drilling rigs. The vessel is commercially engaged in hauling freight, although not on a public carrier basis.

Your next question dealt with vessels eligible for the one-percent assessment ratio under Revenue and Taxation Code, Section 227. Your question dealt with a vessel employed in taking seven or more people out for purposes of scuba diving. Apparently, the vessel has a sport-fishing license which is needed only if the passengers elect to fish rather than scuba dive.

We would recommend that vessels employed in this manner are not eligible for the one-percent assessment. They are not employed exclusively in carrying or transporting seven or more people for hire for commercial passenger fishing purposes. Scuba diving purposes are not the same as passenger fishing purposes.

We might add that for 1980 and subsequent years, carrying seven or more people for fishing purposes is no longer an eligible activity for the one-percent assessment.

Your last question asked whether amended Revenue and Taxation Code, Sections 6368 and 6368.1 should be used in determining if a vessel qualified for the one-percent assessment ratio as a commercial fishing vessel. Sections 6368 and 6368.1 provide criteria for use in determining whether a vessel is exempt for sales and use taxes. These sections do not apply for property tax purposes.

Sincerely,

Buddy W. Florence
Senior Property Auditor-Appraiser
Assessment Standards Division

BWF:dg
cc: Honorable George R. Reilly
Mr. Gordon P. Adelman